

# PHILIPPINES ECONOMIC WRAP-UP

JULY 22-28, 2000

## ----- Summary -----

In addition to our regular reports on forex markets, interest rates and the Philippine stock markets, this week we report on President Estrada's proposed P725 billion budget for 2001. The May survey on manufacturing reveals inconsistent (but positive) growth in the sector. We provide an update on the privatization of Philippine National Bank among other banking news. There is suspicion of a new scandal at the Philippine Stock Exchange. The government is seeking to defer implementation of the Clean Air Act after considering the costs. And the government is fighting a proposal to create an "oil exchange" to counter energy price hikes.

These weekly reviews are available on the Embassy's web site (<http://usembassy.state.gov/manila>). We provide a longer and more detailed review of the Philippine economy in our May Economic Outlook, which can also be found on our web site.

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## ----- Market and Policy Developments -----

# FOREX REPORT

The Philippine peso, which sank to trade as low as P45.195/USD this week, was able to stage a modest recovery as government officials assured traders that the current depreciation was temporary and in line with regional currency troubles. Executive Secretary Ronnie Zamora suggested at one point that perhaps now was the time for the Bangko Sentral ng Pilipinas to intervene in the market to prop up the currency, but BSP Managing Director Amando Tetangco told reporters that the BSP would only intervene if needed to prevent sharp fluctuations in the peso's value. On July 28, the peso closed at P44.86/US\$; the July 21 close was P44.40/US\$.

## Exchange Rate Tables

Date	Weighted Average (Pesos/US\$)	Closing (Pesos/US\$)	Volume (Million US\$)
JUN 19	42.649	42.655	93.5
20	42.672	42.675	142.6
21	42.693	42.830	86.0
22	42.907	42.870	128.0
23	42.879	42.845	76.0
JUN 26	42.890	42.910	73.0
27	42.963	43.020	63.0
28	43.115	43.130	97.1
29	43.154	43.170	114.6
30	43.253	43.230	108.6
JUL 03	43.436	43.530	98.1
04	43.563	43.535	89.0
05	43.646	43.690	77.5
06	43.851	43.950	123.1
07	43.981	44.030	96.4
JUL 10	44.116	44.305	91.3
11	44.769	44.820	146.3
12	44.866	44.665	162.4
13	44.567	44.705	145.3

14	44.559	44.520	184.0
JUL 17	44.543	44.590	90.0
18	44.622	44.540	106.9
19	44.456	44.510	105.5
20	44.552	44.585	94.5
21	44.510	44.400	121.0
JUL 24	44.529	44.600	108.0
25	44.692	44.755	118.6
26	45.028	45.070	122.5
27	44.989	44.875	125.2
28	44.941	44.860	128.0

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Source: Bankers Association of the Philippines

#### CREDIT MARKET REPORT

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The Treasury Bureau of the Bangko Sentral ng Pilipinas (BSP, the central bank) finally let interest rates on Treasury bills rise, and on full awards for all maturities, the increases were fairly moderate. At the July 24 auction, the interest rate on the 91-day T-Bill rose 2.9 basis points to 8.919%; the 182-day rate rose 3.7 basis points to 10.00%, and the 364-day T-Bill interest rate rose 2.1 basis points to 11.010%. Results at the July 25 auction of 2-year Treasury bonds were similar; a 25 basis point hike from the June 30 auction saw rates for the two-year paper rise to 12.125%. Traders expect the government's borrowing needs to increase as deficit targets continue to slip.

The Philippine government is selling "privatization bonds" to small investors to help finance its projected P62.5 billion budget deficit. The government had planned to raise some P22 billion through privatization efforts in 2000, but the so far revenues have fallen far short of targets. Investors will be able to exchange the bonds for shares in the privatized companies. The five-year maturity bonds pay a coupon rate of 375 basis points over Five-year treasury notes.

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# Domestic Interest Rates (in percent)

## Treasury Bills

Auction Date	91 days	182 days	364 days
JUN 19	8.911	10.045	10.924
JUN 26	8.896	9.849	10.685
JUL 03	8.890	9.901	10.796
JUL 10	8.890	no sales	no sales
JUL 17	8.890	9.963	10.989
JUL 24	8.919	10.000	11.010

Source: Bureau of the Treasury

## Prime Lending Rates of 15 Expanded Commercial Banks

Date of Survey	Average	Range
JUN 22	11.1379	10.00 - 13.625
JUN 28	11.1806	9.50 - 13.625
JUL 05	11.1715	9.50 - 13.500
JUL 12	11.1707	9.50 - 13.500
JUL 20	11.1540	9.50 - 13.500
JUL 27	11.1495	9.50 - 13.500

Sources: Bangko Sentral ng Pilipinas; Press reports

## STOCK MARKET REPORT

The moribund Philippine Stock Market continued to sink as traders expressed fears of higher interest rates, inflation and the sinking peso. Trading volumes were miniscule, averaging only a little over P500 million a day. (The 1999 daily average value of shares traded was over P3 billion.) The 33-share Philippine Stock Index (PHISIX) ended the week at 1437.08, down from its July 21 close of 1479.46. The Phisix is down nearly one-third from its December 30, 1999 close of 2142.97.

Philippine Stock Exchange Index (PHISIX) and  
Value of Shares Traded

Date	PHISIX Close	Value (Million pesos)
JUN 19	1560.67	1001
20	1560.40	1121
21	1555.62	816
22	1545.90	1156
23	1542.97	966
JUN 26	1532.24	628
27	1529.37	925
28	1531.01	873
29	1532.74	767
30	1533.99	938
JUL 03	1535.65	397
04	1538.88	525
05	1539.92	587
06	1542.41	687
07	1550.60	882
JUL 10	1557.57	765
11	1563.08	738
12	1554.57	902
13	1561.52	1321
14	1553.89	641
JUL 17	1546.60	609
18	1528.85	704
19	1516.99	1,233
20	1489.47	832
21	1479.46	952
JUL 24	1477.80	495
25	1481.60	341
26	1478.33	479
27	1448.90	589
28	1437.08	713

Source: Philippine Stock Exchange

## ESTRADA PROPOSES P725 BILLION BUDGET FOR 2001

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President Estrada has proposed a P725 billion budget authorization for calendar year 2001, 11.6% higher than this year's level. According to budget officials, the budget plan prioritizes support for agricultural development and modernization, the promotion of peace and order, and infrastructure spending -- and also recognizes the need to provide funding support for the development of Mindanao. One of the major goals under the 2001 budget proposal is to significantly hike disbursements for foreign-assisted projects. Budget officials said these projects have funding commitments and carry concessional terms, giving the government leeway to incur a higher 2001 fiscal deficit -- envisioned at P85 billion (versus 2000's P62.5 billion program) -- without unduly crowding out the private sector and pushing up domestic interest rates. Legislators have vowed to carefully scrutinize the government's macroeconomic assumptions and its ability to fund the budget proposal. The head of the Senate's finance committee hinted that another protracted congressional debate was possible. President Estrada signed the 2000 budget into law last February -- a month and a half through the budget year.

## MAY 2000 MANUFACTURING OUTPUT

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The National Statistics Office's (NSO) latest monthly Integrated Survey of Selected Industries (MISSI) estimated manufacturing output to have expanded 12.3% year-on-year in May, after stagnating in April. Sales volume expanded year-on-year for the ninth consecutive month. Although manufacturing output appears headed for a stronger expansion this year, NSO officials observed that production growth since mid-1999 "has moved in three to four-month swings of high-low-high". The pattern suggests a building-up and running-down approach to inventory management. This may reflect a guarded optimism towards building-up stocks more aggressively. It may also be a reflection of a still tight (albeit improving) credit market, as well as the limited financial ability of manufacturing firms (which have yet to fully recover from the effects of the Asian crisis) to tie-up working capital in inventories.

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MONTHLY INTEGRATED SURVEY OF SELECTED INDUSTRIES  
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	Year-on-Year Change (%)	
	Production Volume	Net Sales Volume
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January 1999	-12.4	-19.0
February	-8.4	-13.8
March	-1.6	-4.9
April	3.5	1.4
May	3.7	-4.4
June	-1.2	-3.0
July	-1.7	-5.8
August	15.2	-4.8
September	5.4	11.9
October	10.8 r/	13.5
November	-4.8 r/	8.9
December	20.3 r/	12.1
January 2000	12.9 r/	20.0
February	7.5 r/	6.3
March	2.8 r/	8.2
April	0.1 r/	10.8
May	12.3 p/	22.5

r/ revised to reflect late survey responses  
p/ preliminary (based on 68.2% response rate)

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Source: National Statistics Office

BANKING NOTES  
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**Philippine National Bank (PNB):** In a special stockholders meeting on July 21, PNB's shareholders approved a reduction in the bank's par value from P100 to P60 per share and the issuance of warrant instruments in connection with the bank's planned P10.3 billion stock rights offering. PNB's president Feliciano Miranda estimated that the upcoming capital infusion (which the bank intends to implement within the next two months) would more than double the bank's capital adequacy ratio from the current 6% to 14%. That would put the bank in compliance with the Bangko Sentral's minimum 10%

requirement. He also indicated that Lucio Tan's group -- which made the sole, winning bid for the government's 30.39% share in PNB on July 19 -- intended to subscribe to the capital hike.

Meanwhile, Department of Finance (DOF) officials said that Lucio Tan's group appeared to be mulling a cash payment (P80/share, a total of almost P5 billion) for the government shares it had acquired. The group had earlier opted for the installment option under the bidding guidelines (P100/share, a total of 6.2 billion payable within two years). The installment option requires the buyer to present a letter-of-credit, which entails additional expenses. The government prefers cash to help keep its fiscal deficit under control. DOF officials told the Embassy that Lucio Tan's group technically has until September 18 to make up its mind -- the deadline set under the bidding guidelines for cash buyers to make full payment and installment buyers to open the required letter-of-credit. If the group sticks with the installment payment, DOF officials said the government could consider discounting the letter-of-credit.

**Upcoming Merger:** Bangko Sentral Governor Rafael Buenaventura announced a planned merger between Banco de Oro and Dao Heng Bank's 60%-owned local subsidiary. Both banks reportedly are concluding their due diligence audit and finalizing a merger deal to be submitted for the approval of the Monetary Board (Bangko Sentral's highest policymaking body). Banco de Oro is controlled by mall taipan Henry Sy.

#### PSE PROBE ON REYNOLDS PHILIPPINES

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Unusual movements in the trading volume of Reynolds Philippines Corporation's (RPC) otherwise lethargically-traded stock has triggered a probe by the Philippine Stock Exchange (PSE). Initial findings by the PSE's Compliance and Surveillance Group (CSG) point to the possibility of "kiting" and "wash sales" involving RPC, its related/affiliated companies, company officers, and PSE member-brokers. PSE officials told the Embassy that the parties concerned will be given "due process" and have been asked to present their respective sides on the CSG's initial findings.



Being financially strapped and debt-saddled appears to have heightened speculation on the aluminum maker's involvement in the suspected schemes as a means of generating much-needed funds. RPC is currently negotiating with creditors for a debt restructuring plan and is reportedly in discussions with a potential investor. PSE officials commented that the scope and intent of the suspected violations appear to differ from the much-publicized BW Resources case -- where the alleged, primary objective was to artificially jack up prices, induce active public trading, and deliberately mislead the investing public.

#### CLEAN AIR ACT IMPLEMENTATION FACES DELAY

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Thirteen months after passing the Clean Air Act of 1999, the government hopes the implementing rules and regulations (IRR) which will fully implement R.A. 8749 would be finalized next month (August). A public awareness campaign on the health benefits of clean air effectively prepared the general public for the implementation of the Act. The first activity to be effected under the Act was the phase-out of leaded gasoline, which was accelerated to April 1 in Metro Manila where motor vehicles account for 50% of the country's gasoline consumption. The oil companies have evidently supported this government effort. But it will take a lot more for them to conform to improved standards for gasoline and diesel fuel as a major step to improve air quality. The country's existing power plants and industrial factories would also need to conform to specific environmental standards. (The pollution standards set by the Clean Air Act, patterned after California's emission standards, are unrealistically stringent, given existing facilities in the Philippines.)

The Department of Energy (DOE) has sounded an alarm to defer implementation of the Act. A preliminary DOE study showed that new requirements for lead and sulfur levels in motor gasoline and diesel fuel by 2003 would increase refining costs and substantially raise pump prices. The three oil companies in the country claim they will need some \$2 billion in new investments in order to meet environmental regulations. Existing geothermal power

plants would require substantial investments to reduce the sulfur content in natural steam. The DOE has proposed that the group formulating the IRR await completion of an Asian Development Bank study on pollution standards. That may help the group address flexibility issues on the performance of the country's existing plants and equipment.

The Board of Investments (BOI) is similarly concerned that new emission standard requirements for industries will require new, mostly imported, equipment and technology. The ban on the use of incinerators caught many industries unprepared. The Philippines lacks hazardous waste handling and processing facilities, and there are few alternative waste treatment facilities in the country. These problems are already affecting investment decisions for plant expansion and new projects, according to BOI. The BOI suggests, but did not specify, a transition period during which existing industries will shift to new waste treatment technologies.

#### PRICE HIKES TRIGGER CALLS FOR "OIL EXCHANGE"

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The "big three" oil companies (Petron, Caltex and Shell) on July 25 raised prices of all petroleum products by 55 centavos/liter (4.62 cents/gal). That was the second time this month and the thirteenth increase in 15 months, since the downstream oil industry was fully deregulated. For one liter of unleaded gas, motorists are now paying PhP16.89 (\$1.42/gal), up 50% from 15 months ago. Petron Corporation's president has said fuel prices could go up again in August because the July price increases were based on the cost of crude and peso exchange rate for the month of June. On July 3, the peso depreciated further to P44/\$ and prices of Dubai crude rose to \$28/barrel. Recent improvements in world crude prices, which averaged \$26.83 in the first three weeks of July would just be enough to offset the peso's recent deterioration, the Petron official claims.

Following the series of fuel price increases, taxi operators have been authorized to raise fares. Buses and jeepney drivers and operators associations have filed petitions with government regulators to increase minimum

fares by at least 33 percent. The country's largest labor organization, the Trade Union Congress of the Philippines, has announced plans to ask for at least a 13% increase in the minimum wage. The Consumer and Oil Price Watch Group, led by industrialist Raul Concepcion, has warned that the July 25 fuel price increase should be the last for this year, given a substantial drop in crude prices breaching the \$25/barrel level in mid-July. Another fuel price increase will spur corresponding adjustments on the prices of basic commodities, Mr. Concepcion added.

To offer relief to consumers burdened by the spiraling cost of fuel products and the projected increases in transportation fares and consumer goods prices, Bataan Representative Enrique Garcia has proposed a bill (HB 8710) for the government to establish an international oil exchange. Under the proposal, the oil exchange would bid out on a monthly basis to more than 40 local and foreign oil refineries and traders the country's total requirements for gasoline, diesel, kerosene, LPG and other refined petroleum products. House Speaker Manuel Villar has publicly stressed that the House will give priority to the proposed measure. Vice President Gloria Macapagal Arroyo is pushing for the creation of an oil exchange to help bring down fuel prices.

DOE Secretary Mario Tiaoqui, however, commented that setting up an oil exchange would run counter to the government's policy of attracting private sector in a deregulated industry. President Estrada initially threw his support behind Garcia's bill but later withdrew it after Tiaoqui and members of the Economic Coordinating Council (ECC) objected to the proposal. The ECC pointed out that the proposal "involves the takeover of all terminals and storage depots for refined petroleum products all over the country." However, the proposed takeover is not feasible because of the staggering amount required for facilities.

The bill has not moved in Congress.